details of that plan to evaluate whether it provides a sufficient incentive for future statutory compliance with Section 271. As the Commission stated in its *NY 271 Order*:

> Where, as here, a BOC relies on performance monitoring and enforcement mechanisms to provide assurance that it will continue to maintain market-opening performance after receiving section 271 authorization, *we will review the mechanisms involved to ensure that they are likely to perform as promised.* While the details of such mechanisms developed at the state level may vary widely, *we believe that we should examine certain key aspects of these plans to determine whether they fall within a zone of reasonableness, and are likely to provide incentives that are sufficient to foster post-entry checklist compliance.*

NY 271 Order ¶ 433 (emphasis added). *See also Texas 271 Order* ¶ 423; *KS/OK 271 Order* ¶ 273.

Although the Commission has not delineated all criteria that a particular enforcement plan must satisfy in order to constitute a sufficient incentive to the BOC to comply with Section 271 in the future, it has identified certain "important characteristics" that increase the likelihood that the enforcement mechanisms in a PAP "will be effective in practice." *NY 271 Order* ¶ *433*. Thus, in the *NY 271 Order*, the Commission determined that the New York PAP would serve as an effective mechanism for ensuring "marketing-opening performance" by Verizon after it received Section 271 authorization, because it contained the following characteristics:

- potential liability that provided a "meaningful and significant incentive to comply with the designated performance standards";
- "clearly-articulated, pre-determined measures and standards" which encompass a "comprehensive range of carrier-to-carrier performance";
- "a reasonable structure that is designed to detect and sanction poor performance";

- a self-executing mechanism "that does not leave the door open unreasonably to litigation and appeal"; and
- "reasonable assurances that the reported data is accurate."

NY 271 Order ¶ 433.[11]

Contrary to Verizon's claim, Verizon is not subject to self-executing performance mechanisms that will assure compliance with its statutory obligations after Section 271 approval. First, the Vermont PAP does not provide a "meaningful and significant incentive to comply with the designated performance standards." *NY 271 Order ¶ 433*. In this regard, the performance remedy plan that Verizon initially proposed to the VPSB was based, in significant measure, on the New York PAP. Kalb Decl. ¶ 11. Consistent with the approach in New York, Verizon's proposed Vermont PAP extended bill credits to CLECs that were directly affected by performance failures associated with all three categories of measures under the plan: (1) Mode of Entry ("MOE") measures; (2) Critical Measures; and (3) Special Provisions Measures. *Id.* ¶ 12. However, the VPSB modified Verizon's proposal by requiring Verizon to make remedy payments to the *State* for those performance failures associated with the Mode of Entry measures in the plan. Significantly, although the CLECs are compensated for performance misses associated with the 12 Critical Measures categories and the few Special Provisions measures, CLECs are *not* compensated for performance failures associated with scores of Mode of Entry measures in the Vermont PAP. This approach is untenable. *Id.* at ¶¶ 13-24.

No performance remedy plan can foster competition and deter anticompetitive conduct effectively if the CLECs which are victimized by such conduct suffer severe financial

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[11] *See also, Texas 271 Order ¶¶ 424-429; KS/OK 271 Order ¶¶ 273-278; Massachusetts 271 Order ¶¶ 240-247.*

consequences resulting in their loss of market share or exit from the marketplace. The Vermont PAP has precisely such an effect because it fails to compensate CLECs for performance misses attributable to the vast majority of measures in the plan. *Id.* ¶¶ 16, 23. Indeed, in apparent recognition of the importance of compensating CLECs that are harmed by the ILEC's substandard or discriminatory conduct, the performance enforcement plans in New York, Connecticut, Massachusetts, Texas, Kansas and Oklahoma require bill credits or payments to CLECs for performance misses associated with *all* or the *vast majority* of the measures in those plans. *Id.* ¶¶ 17-23. Because the Vermont PAP does not compensate CLECs for Verizon's performance failures on scores of metrics contained therein, it cannot promote competition or deter anticompetitive conduct effectively. *Id.* ¶ 13.

Second, the Vermont PAP is also fundamentally flawed because it cannot effectively detect discrimination. *Id.* ¶¶ 25-30. The Vermont PAP contains a statistical confidence interval that is biased in Verizon's favor. By using a 95% one-tailed confidence interval, the Vermont PAP fails properly to balance the risk of Type I error (a finding that discrimination has occurred when in fact it has not) against the risk of Type II error (a finding that no discrimination has occurred when in fact it has). By only accounting for and holding the risk of Type I error to 5%, the Vermont PAP substantially increases the risk of a Type II error which disadvantages CLECs. Thus, the statistical methodology in the Vermont PAP is skewed in favor of Verizon. *Id.* ¶ 29.

For all of these reasons, the Vermont PAP does not provide appropriate self-executing enforcement mechanisms sufficient to detect or deter anticompetitive conduct in the wake of Section 271 relief.

III. VERIZON'S ENTRY INTO THE INTERLATA MARKET IS NOT CONSISTENT WITH THE PUBLIC INTEREST.

There is a final, independent reason why the Commission should deny Verizon's application. Even if the Commission could rationally find that Verizon had fully implemented its obligations under the competitive checklist, including its duty to set cost-based rates within the range that a reasonable application of TELRIC would produce or to provide nondiscriminatory access to its operations support systems, the record here precludes any finding that granting Verizon's application is "consistent with the public interest, convenience and necessity." 47 U.S.C. § 271(d)(3(C)).

The reason is straightforward. At the heart of the public interest inquiry, as Congress conceived it and as this Commission has explained, is a determination of whether, notwithstanding checklist compliance, the local market is in fact fully open to competition. Unless the Commission can confidently make such a determination, any grant of interLATA authorization is not only premature but wholly at odds with the fundamental premise of the Act.

The first step in the public interest inquiry is therefore to assess the actual state of local competition. Here the record shows that competition from facilities-based or UNE-based competitors is almost non-existent. In particular, little more than 1% of all switched access lines in Vermont are served by facilities-based competitors, and less than 3/10 of 1% of such lines are served by UNE-based competitors. There is even less competition for residential service – a mere 287 lines, or less than 2/10 of 1% of the residential lines in Verizon's Vermont service territory, are served by facilities-based competitors, and *only 58 lines*, less than 1/10 of 1% of such lines, are served by UNE-based competitors. The record confirms, moreover, that the absence of virtually any facilities or UNE-based competition is *not* the result of neutral business considerations uniquely within the control of new entrants, *Michigan 271 Order* ¶¶ 385-391, but, as explained above, is due to Verizon's anticompetitive resistance and refusal to open local markets in Vermont to competitors. Accordingly, approval of this joint application is not in the public interest.

A. InterLATA Authorization Is Not In The Public Interest Unless The BOC's Local Markets Are Irreversibly Open To Competition.

As a threshold matter, Verizon "disagrees as a legal matter that the Commission may conduct any analysis of local competition in its public interest inquiry." Verizon Br. at 75 n.64. The Commission has previously considered and flatly rejected the argument once again advanced by Verizon:

> "We reject the view that our responsibility to evaluate public interest concerns is limited narrowly to assessing whether BOC entry would enhance competition in the long distance market. We believe that our inquiry must be a broader one. The overriding goals of the 1996 Act are to open all telecommunications markets to competition by removing operational, economic, and legal barriers to entry, and, ultimately, to replace government regulation of telecommunications markets with the discipline of the market. In order to promote competition in the local exchange and exchange access markets in all states, Congress required incumbent LECs, including the BOCs, to provide access to their networks in a manner that allows new entrants to enter local telecommunications markets through a variety of methods. In adopting section 271, Congress mandated, in effect, that the Commission not lift the restrictions imposed by the MFJ on BOC provision of in-region, interLATA services, until the Commission is satisfied on the basis of an adequate factual record that the BOC has undertaken all actions necessary to assure that its local telecommunications market is, and will remain, open to competition."

Michigan 271 Order ¶ 386. *See also Massachusetts 271 Order* ¶ 233 ("we may review the local and long distance markets to ensure that there are not unusual circumstances that would make entry contrary to the public interest under the particular circumstances of this application").

Accordingly, the key question to be resolved in the public interest inquiry is whether the BOC's local markets truly "are open to competition" from new entrants. *See, e.g.*, *Kansas/Oklahoma 271 Order* ¶ 267. Meeting the checklist requirements alone is merely a necessary, but not a sufficient, predicate to demonstrate that local markets are in fact open. Section 271(d)(3) requires an additional and independent finding that entry is in the public interest. *E.g.*, *Michigan 271 Order* ¶ 389. The public interest test reflects Congress' recognition that, at least in some circumstances, mere satisfaction of the checklist would not be sufficient to allow local competition to develop, and that if the BOCs in those states nevertheless received long distance authority they would leverage their local monopoly into the long distance market – precisely the harm that the ban on interLATA service in section 271(a) is designed to prevent. *See id.* ¶ 388 ("local telecommunications markets must *first* be open to competition so that a BOC cannot use its control over bottleneck local exchange facilities to undermine competition in the long distance market") (emphasis added).

Thus, to determine whether the BOC's local telecommunications markets are in fact open to competition, the Commission first reviews the extent to which new entrants "are actually offering" local service to both business and residential customers through each of the three means offered by the Act. *Id.* ¶ 391. Second, where local competition is not securely established, the Commission determines whether this reflects the continuing presence of entry barriers and BOC misconduct, or is attributable instead solely to the business decisions of potential new entrants.

B. Verizon Maintains Monopoly Power Over Residential Service.

The "Act contemplates three paths of entry into the local market – the construction of new networks, the use of unbundled elements of the incumbent's network, and resale" (*id.* ¶ 96). Congress "sought to ensure that all procompetitive entry strategies are available." *Id.* ¶ 387. As the Commission has recognized, its "public interest analysis of a section 271 application, consequently, *must* include an assessment of whether all procompetitive entry strategies are available to new entrants." *Id.* (emphasis added). And, as the Commission explained in the *Michigan 271 Order*, "[t]he most probative evidence that all entry strategies are available would be that new entrants *are actually offering* competitive local telecommunications services to different classes of customers (residential and business) through a variety of arrangements (that is, through resale, unbundled elements, interconnection with the incumbent's network, or some combination thereof), in different geographic regions (urban, suburban, and rural) in the relevant state, and at different scales of operation (small and large)." *Id.* ¶ 391 (emphasis added). In subsequent applications, the Commission has repeatedly considered the degree to which competitors have actually succeeded in offering local telecommunications services using the different entry strategies prescribed by the Act. *See, e.g., New York 271 Order* ¶¶ 13-14; *Texas 271 Order* ¶¶ 5-6.

Here, Verizon's own data confirm that facilities-based and UNE-based entry is almost non-existent in Verizon's Vermont service territories. Using the E911 data presented by Verizon witness Paula L. Brown, Tables 1 and 2 show the amount of CLEC competition in Vermont. The data in Table 1 show that barely over 1% of all switched access lines in Vermont are served by facilities-based competitors, and less than 3/10 of 1% are served by UNE-based competitors. The data in Table 2 shows that there is even less competition for residential service – a mere 287 lines, or less than 2/10 of 1% of the residential lines in Verizon's Vermont service territory, are served by facilities-based competitors, and only 58 lines, less than 1/10 of 1% of such lines, are served by UNE-based competitors.

TABLE 1: Total CLEC Penetration in Verizon-VT's Service Territory

	Quantity	**Share**
Verizon VT Retail Switched Access Lines[12]	350,000	94.22%
CLEC Facilities-Based Lines[13]	4,778	1.29%
CLEC UNE Lines[14]	786	0.21%
CLEC Resale Lines[15]	15,900	4.28%
Total Lines in Verizon VT Service Territory	371,464	100.0%

TABLE 2: Residential Market CLEC Penetration in Verizon-VT's Service Territory

	Quantity	**Share**
Verizon VT Retail Residential Switched Access Lines[16]	222,050	99.69%
CLEC Residential Facilities-Based Lines[17]	287	0.13%
CLEC Residential UNE Lines[18]	58	0.03%
CLEC Residential Resale Lines[19]	342	0.15%

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[12] Brown Decl. Attachment 1, ¶ 3.

[13] Brown Decl. Attachment 1, Table 1.

[14] Brown Decl. Attachment 1, Table 1.

[15] Brown Decl. Attachment 1, Table 1.

[16] Verizon reports that it serves 350,000 lines in Vermont, without providing a break-down between residential and business lines. Brown Decl. Attachment 1, ¶ 3. To extrapolate the percentage of Verizon's total switched lines in Vermont that are provided to residential customers, we have relied on data reported by Verizon to the Commission as of December 31, 2000, indicating that of the 7,241,653 total switched access lines served by Verizon New England Inc. (which includes Massachusetts and Vermont), 4,655,604, or 64.3%, were residential access lines. FCC, Statistics of Communications Common Carriers as of December 31, 2000, at Table 2.6 (September 1, 2001). 64.3% of 350,000 is 222,050.

[17] Brown Decl. Attachment 1, Table 1.

[18] Brown Decl. Attachment 1, Table 1.

Total Residential Lines in Verizon VT Service Territory		100.0%

Moreover, even these minuscule shares present an overly optimistic picture of likely future CLEC competition in Vermont. To begin with, as reflected in Table 3, many of the facilities-based CLECs that Verizon identifies as its competitors in Vermont,[20] have gone, or are going, out of business or are otherwise in financial distress at the present time.

TABLE 3: Current Financial Status of Facilities-Based Vermont CLECs Identified By Verizon[21]

VT Facilities-Based Providers	**Change in Mkt. Cap.**	**Current Financial Situation**
Adelphia Business Solutions	- 98.66%	Spun off by parent Adelphia Communications with $1.4 billion debt which analysts predict will force into sale, radical restructuring, or bankruptcy; announced in January 2002 no dividend payments forthcoming on preferred stock following Salomon Smith Barney report that it faces "near-term restructuring or bankruptcies;" rumors of impending bankruptcy have caused stock to plunge and cut off new capital.
Z-Tel	- 58.97%	Reported 3rd Quarter 2001 loss of $26 million and $156.9 million loss for first 9 months of year 2001; cut customer base by 13% in 3rd Quarter 2001; eliminated over 40% of its workforce, ceased telemarketing, wrote off 80,000 deadbeat subscribers at cost of $30 million; significantly slowing its acquisition of new subscribers and its expansion into new markets; reported year 2000 loss of $111.7 million.
AT&T	- 24.04%	Announced in January 2002 plans to record $1 billion 4th Quarter 2001 restructuring charge and expects to eliminate 5,000 employees in 2002, after cutting 8,000 in 2001.
DSL.net	- 74.51%	Reported 3rd Quarter 2001 net loss of $10.4 million; Nasdaq contacted in July 2001 regarding possible delisting; applied to FCC in July 2001 to discontinue interstate special access DSL service for high-speed Internet access in 22 states; reported 2nd

[19] Brown Decl. Attachment 1, Table 1.

[20] Brown Decl. Attachment 1 at 7-10.

[21] Table 3 is derived from Attachment 4 hereto.

		Quarter 2001 net loss of \$23.6 million, and 1st Quarter net loss of \$25.7 million; announced in July 2001 elimination of 90 jobs and closing of 250 operational central offices, and expects to record a loss of \$80 to \$90 million in 2001.
StarBand		Laid off 30% of employees in 2001, and has not made a profit for investors due in part to slower than expected demand.
Hughes Electronics Corp.		Reported year 2001 net loss of \$621.6 million, 4th Quarter 2001 net loss of \$132.6 million, and has agreed to sell its DirecTV satellite television unit to EchoStar Communications Corp; satellite Internet subsidiary (Hughes Network Systems) laid off 200 workers in December 2001, cut forecasts for new subscribers and reported negative 3rd Quarter 2001 EBITDA of \$22.6 million.

The prospects for increased UNE-based competition are also bleak. UNE-based entry into residential service will also be impaired so long as UNE rates remain above TELRIC and above a level that would permit competitive entry. If Verizon actually offered CLECs non-discriminatory access to the full economies of scale in its existing network, the Commission should see meaningful entry by and increasing competition from UNE-based entrants. Yet, since the passage of the Act, all CLECs combined in Vermont have managed to gain just 786 UNE-based lines and only 58 UNE-based residential lines. The microscopic level of UNE-platform-based entry in Vermont is by degrees of magnitude smaller than the level achieved in other Verizon states in which the Commission has granted section 271 applications. As reflected in Table 4, the current level of UNE-based competition for residential service in Verizon's Vermont service territory is *less than 1 percent* of the levels of UNE-based residential competition that existed in Massachusetts, New York and Pennsylvania at the time the Commission considered section 271 applications for those states.

TABLE 4: VT Versus Other States – CLEC Residential Entry Via Facilities and UNE-P

	Vermont	**NY**[22]	**PA**[23]	**MA**[24]
UNE-P	58	137,342	197,000	8,050 (approx)
Facilities	287	35,753	95,000	80,000 (approx.)
TOTAL	**345**	**173,095**	**292,000**	**88,050 (approx.)**

Finally, resale is an inherently limited competitive vehicle, both because resale-based competitors cannot alter the nature of the service they are reselling (and thus cannot provide competitors with innovative or improved services), and because resale is priced in a manner that precludes its use in all but the most selectively chosen circumstances.[25] The record thus shows that resale is not a growing, viable source of future competition for Verizon in Vermont, and that no entrant has yet succeeded in using either UNEs or facilities to offer competitive local residential service.

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[22] *New York 271 Order* ¶ 14.

[23] *Pennsylvania 271 Order* at n. 260; *Application of Verizon Pennsylvania Inc., et al. for Authorization To Provide In-Region, InterLATA Services in Pennsylvania,* FCC 01-269, at 52 (June 21, 2001); Comments of AT&T Corp., *Application of Verizon Pennsylvania Inc., et al. for Authorization To Provide In-Region, InterLATA Services in Pennsylvania,* CC Docket No. 01-138, at 71 (filed July 11, 2001) (citing to Verizon Witness Taylor, Att. 1, Exhibit B).

[24] *Massachusetts 271 Order* ¶ 64.

[25] The avoided cost discount has proved inadequate to provide CLECs a basis for profitable entry for most consumers. For example, as monopolists, the incumbents do not face (and therefore do not "avoid") the huge customer acquisition costs that CLECs confront, nor do they face the lack of economies of scale that a new entrant must address. And CLECs providing resale do not benefit from access revenue. For all of these reasons, CLECs seeking to provide a broad-based, significant competitive alternative to the incumbents' local residential monopoly cannot do so through the resale of local service.

C. The Record Demonstrates That Verizon's Local Residential Markets Remain Closed To UNE- and Facilities-Based Competition.

Because the relevant data show a lack of meaningful local competition, the Commission must next determine "whether the lack of competitive entry is due to the BOC's failure to cooperate in opening its network to competitors, the existence of barriers to entry, the business decisions of potential entrants, or some other reason." *Michigan 271 Order* ¶ 391. To make this determination, the Commission should consider all "relevant factors" that might "frustrate congressional intent that markets be open [to competition]." *Kansas/Oklahoma 271 Order* ¶ 267. A review of the evidence makes clear that entry barriers and Verizon's own actions have perpetuated Verizon's monopoly over residential service in Vermont.

Verizon continues to discriminate against CLECs in the provision of interconnection and UNEs in ways that directly impair CLECs' ability to compete. As discussed above, Verizon has failed to establish reliable performance measures and an effective enforcement plan, both of which are crucial to the ability and willingness of new entrants, particularly UNE-based competitors, to incur the substantial investment required to enter a BOC's local market, as well as to the continuing viability of competition once entry has occurred. *E.g., Michigan 271 Order* ¶¶ 393-94.

Further, the evidence here shows not only that Verizon's UNE rates in Vermont are not TELRIC-compliant, but also that those rates are so high that they preclude efficient local entry. Specifically, those rates effect a price squeeze that prevents UNE-based competitors from earning sufficient margins to provide local service economically in competition with Verizon, by imposing wholesale costs on Verizon's competitors that render it impossible for them to offer a retail service that would be price competitive. *See* Lieberman Decl. ¶¶ 32-47.

Verizon's imposition of rates that foreclose broad-based local competition has two independent legal consequences in this proceeding. *First*, as described above, it establishes that those rates violate Checklist Item 2 because they are discriminatory. *Second*, the direct evidence of a price squeeze also establishes that granting the application could not be consistent with the "public interest." 47 U.S.C. § 271(d)(3)(C). The Supreme Court has explained that the statutory term "public interest" "take [its] meaning from the purposes of the regulatory legislation." *NAACP* v. *FPC*, 425 U.S. 662, 669 (1976). The central purpose of Section 271 is to ensure that local telephone markets in a State are open to competition – and that competing carriers therefore have the legal and economic ability to provide competing local services – before a BOC in that State is permitted to provide long-distance services. As the Commission has held, Congress adopted Section 271 in order to assure that BOCs could not provide long distance service at a time when their local monopolies would give them an "unfair advantage" over long distance competitors in, *inter alia*, providing "combined packages" of local and long distance service to customers who desire "one-stop shopping." *AT&T* v. *Ameritech*, 13 F.C.C. Rcd. 21438, ¶¶ 5, 39 (1998), *aff'd sub nom. U S WEST* v. *FCC*, 177 F.3d 1057 (D.C. Cir. 1999). If, by contrast, long-distance entry were allowed before other carriers could provide competing combined packages, it would "threaten competition" in both the local and the long-distance markets by granting the BOC a monopoly in the provision of such combined services. *Id.* ¶ 5. The Commission has thus held that the "public interest" prong of Section 271 requires it to "ensure that no other relevant factors exist that would frustrate the congressional intent that markets be open." *Kansas/Oklahoma 271 Order* ¶ 267. A price squeeze that would foreclose efficient local entry into the residential market obviously constitutes such a "relevant factor."

And proof that such a factor in fact exists demonstrates conclusively that the market is not – and cannot be – open.

The Commission nonetheless had previously held that it need not consider evidence of a price squeeze in evaluating a Section 271 application. That holding was based on the Commission's view that such evidence was "irrelevant," and that considering it would improperly involve the Commission in the process of setting local retail rates that are outside its jurisdiction. *Id.* ¶ 92. But the Court of Appeals for the D.C. Circuit, relying on the Supreme Court's decision in *Conway*, has now squarely rejected that view. *Sprint* v. *FCC*, 2001 U.S. App. LEXIS 27292 (D.C. Cir. 2001). Indeed, because the central purpose of the 1996 Act is "stimulating competition," the D.C. Circuit held that the "public interest" analysis under Section 271 may weigh even "*more heavily* towards addressing potential 'price squeeze'" than was required under the Federal Power Act in *Conway*. *Id.*, at *15 (emphasis added).

Moreover, the *Sprint* Court also confirmed that the Commission's lack of jurisdiction over retail rates was no bar to such an analysis, because the Commission can respond to a price squeeze without disturbing retail rates. Instead, because the Commission has said that TELRIC rates exist within a "band," one entirely permissible solution is to "'fix[] the wholesale rates, which [a]re under its jurisdiction, at a lower level within'" that band. *Id.* at *12 (citing *Conway*, 426 U.S. at 279). Here, because, as AT&T has shown, Verizon's rates are not TELRIC-compliant to begin with, there is certainly plenty of room for downward movement.

Under *Sprint* v. *FCC*, therefore, when evidence is presented in a Section 271 proceeding that UNE-based residential competition is economically infeasible, the Commission cannot grant that application without evaluating and addressing that evidence. Unless the

Commission rejects this application on other grounds, therefore, it must develop and apply a framework in this proceeding for analyzing such price squeeze claims.

In the face of the D.C. Circuit's *Sprint* decision, Verizon raises several arguments, none of which have merit.

First, Verizon asserts that "the Commission is under no obligation to analyze whether the UNE rates in Vermont could conceivably permit a price squeeze." Verizon Br. 88. Verizon's remarkable invitation squarely conflicts with the *Sprint* decision, which ordered the Commission to consider "whether the UNE pricing selected here *doomed* competitors to failure" (*id.* at 11, emphasis in original), and the Commission's own recent recognition that Section 271 requires a rational framework for consideration of the price squeeze issue.[26]

Second, Verizon claims that it is legally irrelevant that UNE-P purchasers cannot economically provide service under Verizon's existing UNE rates in Vermont. Verizon relies on antitrust cases that purportedly hold that a price squeeze can exist only if "essential inputs" are not available at a "fair price." Verizon Br. 89. Verizon claims that this standard cannot be met here because UNE prices are necessarily "fair" if they have been found to fall within the range that satisfies TELRIC. In all events, Verizon claims that UNE-P is in no way an essential input in that the Act makes available resale under § 251(c)(4) and a variety of other means in which to gain access to Verizon's network. These claims are baseless.

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[26] In recognition of the need to develop and apply such a framework in Section 271 proceedings where such claims are made, the Commission recently asked the Court of Appeals for the D.C. Circuit to suspend briefing in the appeal of its order granting Verizon interLATA authority in Massachusetts. The Commission asked for that suspension so that it could address the price squeeze claims that had been made in that proceeding but that the Commission's order had not

As an initial matter, Verizon misstates the applicable antitrust decisions. *Alcoa* holds that a firm with monopoly control over an input essential to the provision of a finished product is engaged in a price squeeze and is not charging a "fair" input price if purchasers of the input cannot make a "living profit" from sale of the finished product – as purchasers of UNEs plainly cannot in Vermont. *United States* v. *Aluminum Co. of America,* 148 F.2d 416, 436-38 (2d Cir. 1945). In *Town of Concord* v. *Boston Edison*, 915 F.2d 17 (1st Cir. 1990), the court held that allegations that electric utilities have set wholesale rates to effect a price squeeze "generally" will not state claims under the antitrust laws because, among other things, the governing regulatory statute requires FERC to determine if a price squeeze will result at the time it reviews the lawfulness of the utility's wholesale rates. *Id.* at 28.

The antitrust decisions are simply besides the point here for a similar reason. Whether or not Verizon is also violating antitrust standards, § 271 bars the Commission from granting Verizon long distance authority unless the Commission finds (1) that the UNE rates are "nondiscriminatory" as well as cost-based (§§ 252(d)(1), 271(c)(2)(B)(ii) & (d)(3)(A)) and (2) that the grant of the application is in the "public interest." § 271(d)(3)(C). As described above, in *Conway,* the Supreme Court has held that even if a utility's wholesale rates are within the range of reasonable cost-based rates, the rates are "discriminatory" and "anticompetitive" if they fall at the high end of that range and if they preclude wholesale purchasers from economically competing with the utility's retail services to any class of customers. Thus, if Verizon's high-end UNE rates foreclose UNE purchasers from economically providing residential competition, Verizon is engaged in "discrimination" and has not satisfied checklist item two. Because § 271

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properly addressed. *See* FCC's Emergency Motion for Temporary Suspension of Briefing, *WorldCom* v. *FCC*, No. 01-1198 (D.C. Cir.) (filed January 7, 2002).

categorically bars long distance authorization unless checklist item two has been "fully implemented," Verizon's arguments about the availability of resale or other means of access are irrelevant in this context.

Similarly, Verizon's reliance on the purported availability of resale to respond to evidence that its high UNE prices have doomed UNE-based competitors to failure is also unavailing in the public interest context. To begin with, resale is irrelevant for this purpose. The wholesale discount that has been set in Vermont is wholly insufficient to allow any firm to cover its internal costs of service, and no firm could economically provide local exchange service in Vermont through resale on a broad basis over time.[27] This is borne out by the paltry market shares currently enjoyed by resale-based competitors in Vermont. *See* Tables 1 and 2, *supra*.

More fundamentally, resale would be irrelevant even if the wholesale discount that has been set in Vermont was sufficient, for resale does not give a CLEC access to the "inputs" required to provide long distance service. In particular, firms engaged in resale are entitled to use the BOCs' facilities to provide only exchange service and not exchange access service. *See Local Competition Order* ¶ 873. Resale thus has no effect on the BOCs' monopoly over the exchange access services that originate and terminate all long distance calls, and resale cannot eliminate a BOC's ability to leverage its exchange access monopoly into the long distance market. In this regard, it is ironic that Verizon would here rely on the fact that "the Commission's own lawyer" had advanced this contention at oral argument in *Sprint*. Verizon Br. 89 n. 81. For when the Commission's counsel did so, AT&T's counsel pointed out that

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[27] Most notably, a competitor that provides services using resale is not entitled to receive either USF support or access revenues. Thus, its potential revenues are significantly reduced compared to providers that employ UNE-P.

resale cannot be used to provide exchange access, and the Court told the Commission's counsel that unless he could dispute that fact – as he could not – resale could not be relied on to defeat a price-squeeze claim. Tr. of Oral Argument, *Sprint Communication Corp. v. FCC*, No. 01-1076 pp. 42-46 (D.C. Cir. September 17, 2002).

Nor is there any other entry vehicle that is available to AT&T and other CLECs in Vermont that could allow multiple CLECs to provide residential service throughout the state. As shown above, facilities-based providers serve little more than 1% of all access lines in Vermont and only 287 residential access lines. Under these circumstances, the only theoretical alternative to UNE-P would be an arrangement in which firms would attempt to provide residential service by leasing unbundled loops from Verizon and combining them with the CLECs' switches to provide service. However, such a "UNE-L" strategy is now wholly uneconomic for this purpose in Vermont (and elsewhere). Quite apart from the fact that carriers cannot rationally invest in switches until they have used UNE-P to build up a customer base (*UNE Remand Order* ¶¶ 254-258), Verizon and other BOCs have not deployed technology that allows customers to change from one local exchange carrier to another efficiently and effectively, in mass market quantities and at low cost. Instead, these changes require manual "hot cuts" which are expensive and which have proven impossible for Verizon and other BOCs to administer without causing unacceptable levels of service outages even when UNE-L is used only for low volumes of orders for business customers.

Third, Verizon points to Vermont's rural nature and speculates that the residential market may not be attractive to competitors even if UNE costs are at the lower end of TELRIC. Verizon Br. 90. Verizon's reliance on Vermont's rural nature, however, does not explain why essentially *no* facilities- or UNE-based entry has occurred *anywhere* in Vermont. Indeed, CLECs have captured a far greater percentage of the available residential access lines in *Arkansas*, another heavily rural state,[28] than they have in Vermont.[29] Moreover, even if the provision of local residential service were found to be unprofitable even when all revenues are taken into account, and even when UNEs are priced at the lower end of the range, then that would simply establish that the Section 271 application must be denied. In that case, it would have been shown that the local market is not open to competition, and BOC entry in those circumstances would patently disserve the public interest by enabling the BOC to remonopolize the long-distance market in that State. A denial of such an application would then afford the State regulatory authority the opportunity to consider whether any interest it has in encouraging competitive entry into the local market and further entry into the long-distance market would warrant taking steps with respect to retail rates, or explicit subsidies for the provision of retail service, to make such entry possible.

Finally, Verizon invites the Commission to find that "conducting a price-squeeze analysis is unnecessary because any policy that attempts to force UNE prices down to the lowest possible level is inconsistent with goals of the Act and the Commission to promote facilities-based competition." Br. 90. Verizon's argument, however, is refuted by its own data in this proceeding. There are only 786 UNE-based lines (and only 58 residential UNE-based lines) in the entire State of Vermont. Given these data, there can be no argument that the availability of UNE-based entry in Vermont has somehow deterred facilities-based entry in the State.

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[28] As of 1990, Arkansas percent rural population, 46.5%, was almost double the national average of 24.8%. *See* U.S. Census Bureau, *Urban and Rural Population: 1900 to 1990* (rel. Oct. 1995), at http://www.census.gov/population/censusdata/urpop0090.txt.

In sum, the lack of facilities- and UNE-based CLEC competition for service in Vermont is due to Verizon's "failure to cooperate in opening its network to competitors" and the "existence of barriers to entry," *not* "the business decisions of potential entrants" that are independent of the entry barriers and BOC misconduct. *Michigan 271 Order* ¶ 391. Nothing suggests that potential entrants have decided that the Vermont markets, though open, are simply not worth pursuing, or "that competitive alternatives can flourish rapidly throughout a state." *Id.* ¶ 392. The local markets in Vermont are simply not open to competition, let alone irretrievably open.

D. Approving Verizon's Section 271 Application Before Local Markets Are Open Will Impair Competition.

There is a final reason, independent of the pricing-related arguments advanced above, for rejecting Verizon's application as inconsistent with the public interest. The complete absence of any meaningful competitive entry in Vermont to date, for which Verizon bears significant responsibility, together with the uncertainty as to Verizon's ability to accommodate such entry in the future, precludes any reasonable finding that Verizon's local market is fully open such that competitors can enter if they so wish. The absence of any meaningful local competition in Vermont, which has not been and cannot reasonably be explained by lack of CLEC interest in pursuing this market, is itself a compelling reason to reject the application at this time as inconsistent with the public interest. *See Sprint* v. *FCC*, 2001 U.S. App. Lexis 27292 at * 15.

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[29] In Arkansas, CLECs have captured 8.5 percent of available residential access lines, whereas, as noted above, CLECs have captured only 0.31 percent of all available residential access lines in Vermont.

Granting a section 271 application before any meaningful UNE or facilities-based local competition has materialized is likely to guarantee not only the indefinite continuation of the BOC's local monopoly but the extension of that monopoly into the long distance market – precisely the anticompetitive effect Section 271 was designed to prevent. Such market power, together with the absence of any carrier able to offer customers a package of local, long distance, and advanced telecommunications services comparable to Verizon's, would provide Verizon enormous market power that it could and would wield to raise prices and harm consumers.

These concerns are not speculative. Although Verizon boasts (Verizon Br. at 78) of the alleged competition currently being provided by Texas CLECs, the January 2001 *TPUC Report* on the "Scope of Competition in Telecommunications Markets of Texas" (Attachment 1) reveals that:

- "monopoly power exists . . . in residential and rural markets in Texas" (*id.* at 83; *see* xiii);
- severe financial problems have caused both large and small CLECs to reduce or eliminate their residential service in Texas (*id.* at 55-58, 80-81);
- this lack of competition has permitted SWBT to extend its monopoly into the provision of bundled combinations of local and long distance services, and to *raise* its prices for local services to both residential and business customers (*id.* at x, 62-64, 79, 81);[30] and, given this monopoly power,
- "residential and rural customers are better served by existing price cap regulation of traditional nonbasic local service until more viable and sustainable competitive choices become available to them."[31]

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[30] As described below, SWBT has also recently raised its rates for long distance service.

[31] *Id.* at ix.

Although Verizon cites increasing numbers of long distance customers the BOCs have added in New York and Texas, the TPUC's Report makes clear that, in Texas, this phenomenon reflects the fact SWBT has begun to extend its monopoly in the provision of residential services into the provision of "bundled" combinations of local and long distance services:

> Because Southwestern Bell can now compete for long distance customers in Texas, the company has made a strong push in 2000 to bundle its offerings to provide residential customers with various options for 'one-stop shopping.' . . . Southwestern Bell also gained a sizeable portion of the long distance market just months after offering long distance service for the first time. Southwestern Bell's largest and strongest competitors have not been offering substantial competition in vertical services or in bundling local residential services with long distance or other services and have lost market share in long distance service.

Id. at x.[32]

In sum, TPUC concludes:

> By the end of 2000, SWBT's financial position had strengthened relative to the CLECs. *SWBT's entry into the long distance market has weakened the ability of CLECs to challenge SWBT in local voice service.* Without investor confidence and funding, in the near term CLECs might pose a weaker challenge to SWBT for local wireline voice telephony or in the "one-stop" shopping market than they did in 1998 and 1999. The Commission has noted that in 2000 SWBT raised its prices on a number of vertical services and was successful in rapidly gaining market share in the long distance market, even though it was offering interLATA long distance to only customers who had SWBT as an ILEC.

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[32] *See also id.* at 79 ("SB 560 also granted SWBT the ability to competitively bundle its products. An important additional piece in SWBT's 'one-stop' shopping strategy was SWBT's receiving a favorable recommendation from the Commission on its Section 271 application, leading to FCC approval for SWBT to offer long distance service in Texas in the second half of 2000. SWBT at present has very limited competition in providing bundled services in Texas").

Id. at 81 (emphasis added).

Moreover, there is at least one other highly significant event in Texas that Verizon neglected to mention. Emboldened by its ability to market bundles of local and long distance services without any competition, in February, 2001, SWBT *raised* its residential long distance rates in Texas by 10 to 33 percent. SWBT increased its basic rates for long-distance service by more than 10 percent.[33] SWBT also increased the "discounted rate" for customers who buy other services from SWBT by 33 percent.[34] The rate increase "'highlights the fact that SWBT feels like they are in control and they can set the price,'" said an analyst with Deutsche Banc Alex. Brown.[35]

In sum, contrary to Verizon's claims, events in Texas clearly demonstrate the danger of premature long distance authorization. Although this Commission has noted that Congress did not adopt a market share test for BOC entry into long distance, Congress by no means required the Commission to ignore virtually non-existent CLEC residential market shares. The non-entry into the Vermont market is powerful evidence that Verizon retains its monopoly over local service. The TPUC Report demonstrates what common sense suggests and what Congress prescribed: that if a local market is not yet fully open to competition, consumers will be harmed by the grant of interLATA authorization. Granting a section 271 application in the circumstances presented here is thus fundamentally inconsistent with section 271 and the

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[33] "SWBT Raises Nonlocal Call Rates: Company Says Prices Better Reflect Costs," *The Dallas Morning News*, February 2, 2001.

[34] *Id.*

[35] *Id.*

Consent Decree on which it is based, and is therefore contrary to the public interest as that term must here be construed. *See generally Sprint* v. *FCC*, 2001 U.S. App. Lexis 27292.

Verizon clearly maintains monopoly power over local services in its service areas in Vermont. Permitting Verizon to provide long distance service under these conditions will simply permit Verizon to extend its monopoly into and impair competition in adjacent markets. On this record, Verizon has failed to demonstrate its entry into long distance would be consistent with the public interest.

CONCLUSION

For the foregoing reasons, and the reasons set out in AT&T's initial comments, Verizon's application for interLATA authorization in Vermont should be denied.

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February 6, 2001

CERTIFICATE OF SERVICE

I hereby certify that on this 6th day of February, 2002, I caused true and correct copies of the forgoing Comments of AT&T Corp. to be served on all parties by mailing, postage prepaid to their addresses listed on the attached service list.

Dated: February 6, 2002
Washington, D.C.

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